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No. 91-615

Supreme Court, U.S.

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# In the Supreme Court

OF THE

## United States

OCTOBER TERM, 1991

ALLIED-SIGNAL INC.,  
as successor-in-interest to  
The Bendix Corporation,  
*Petitioner,*

v.

DIRECTOR, DIVISION OF TAXATION  
*Respondent.*

On Writ of Certiorari to the  
Supreme Court of New Jersey

### BRIEF OF PETITIONER

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## QUESTIONS PRESENTED

1. Whether the Due Process and Commerce Clauses preclude a state from imposing a tax on income that a nondomiciliary corporation derives from the sale of its minority interest in another corporation, when the two corporations are not engaged in a unitary business and when the only connection between the taxpayer's minority investment and the taxing state lies in the taxpayer's subsequent use of the proceeds from the sale of its investment.

2. Whether this Court should now clarify, or should additionally articulate, the criteria it has set forth in *ASARCO, Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307 (1982), and related cases, so as to forestall the widespread efforts of states to extend their taxing power well beyond traditional constitutional confines by taxing intangible income with which they have no substantial connection.

## **LIST OF PARTIES**

The parties are as stated in the caption. In the courts below, the taxpayer was referred to as The Bendix Corporation. As appears in the Rule 29.1 Statement, Allied-Signal Inc. has become the successor-in-interest to The Bendix Corporation by successive mergers.

## **RULE 29.1 STATEMENT**

Pursuant to Rule 29.1 of the Rules of this Court, petitioner states that prior to January 31, 1983, The Bendix Corporation had no parent corporation. On January 31, 1983, The Bendix Corporation became a wholly-owned subsidiary of Allied Corporation, which then had no parent corporation. On March 31, 1985, The Bendix Corporation was merged into Allied Corporation. Subsequent to March 31, 1985, and prior to September 30, 1987, Allied Corporation was a wholly-owned subsidiary of The Signal Companies, Inc., which in turn was a wholly-owned subsidiary of Allied-Signal Inc. On September 30, 1987, both of these companies were merged into the parent company, Allied-Signal Inc. Allied-Signal Inc. has no parent corporation. Its non-wholly-owned subsidiaries are listed in Appendix E to the Petition for Certiorari at 72a and, except for the addition of Universal Assets Inc., there are no subsequent changes to the list.

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**BRIEF OF PETITIONER**

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**OPINIONS BELOW**

The opinion of the Supreme Court of New Jersey (Pet. App. A 1a-24a)<sup>1</sup> is reported at 125 N.J. 20, 592 A.2d 536. The opinion of the Superior Court of New Jersey,

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<sup>1</sup> References to the Appendix to the Petition for Certiorari are denominated "Pet. App." followed by a letter assigned to each item and a page reference. References to the Joint Appendix are denominated "J.A." followed by a page reference.

Appellate Division (Pet. App. B 25a-44a), is reported at 237 N.J. Super. 328, 568 A.2d 59. The opinion of the New Jersey Tax Court (Pet. App. C 45a-67a) is reported at 10 N.J. Tax 46.

## **JURISDICTION**

The judgment of the Supreme Court of New Jersey was entered on July 16, 1991. Pet. App. A 24a. The petition for certiorari was filed on October 11, 1991, and was granted on November 27, 1991. The jurisdiction of this Court rests upon 28 U.S.C. § 1257(a).

## **CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED**

The Due Process Clause of the Constitution, amend. XIV, § 1, provides: "[N]or shall any state deprive any person of life, liberty, or property, without due process of law."

The Commerce Clause of the Constitution, art. I, § 8, cl. 3, provides that the Congress shall have power: "[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

Relevant portions of the New Jersey Corporation Business Tax Act, N.J. Stat. Ann. §§ 54:10A-1 *et seq.*, are set forth at Pet. App. D 68a-71a.

## **STATEMENT**

This case concerns the power of a state to tax the capital gain earned by a nondomiciliary corporation from the sale of its minority investment in another corporation with which it had no functional connection and which it



did not control. The precise question here is whether New Jersey may tax a share of the gain that a Michigan-based manufacturing corporation (Bendix) realized from the sale of its 20.6 percent investment in an unrelated metal mining corporation (ASARCO). The facts, which have been stipulated,<sup>2</sup> are not in dispute.

# **1. Bendix's Business**

Petitioner Allied-Signal Inc. is the successor-in-interest to The Bendix Corporation, the original taxpayer in this case. Bendix was a Delaware corporation with its corporate headquarters and commercial domicile in Southfield, Michigan. Stip. ¶¶ 7, 10 (J.A. 154). Formed in 1929 as a manufacturer of aviation and automotive parts, Bendix had evolved by the 1970s into a multinational enterprise with operations in all 50 states. Stip. ¶¶ 7, 11 (J.A. 154-55).

Bendix's business activities were concentrated in four industrial sectors: automotive, aerospace/electronics, industrial/energy, and forest products. Stip. ¶ 11 (J.A. 154-55). All of Bendix's "corporate" (i.e., nonoperating) functions, such as corporate planning, accounting, and management of investments, were based and controlled in Southfield, Michigan. Stip. ¶¶ 7-30 (J.A. 154-61). None of these cor-

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<sup>2</sup> References to the Stipulation of Facts in this case are denominated "Stip." followed by a paragraph reference. The Stipulation of Facts is reproduced at J.A. 152-198. Selected exhibits to the Stipulation of Facts are denominated "Stip. Exh." followed by a letter assigned to each item and a reference to the Joint Appendix.

porate activities was carried on in New Jersey. Stip. ¶¶ 31-38a (J.A. 161-63).

Bendix's activities in New Jersey consisted primarily of the operation of several units in the aerospace/electronics group (flight systems, guidance systems, and test systems) and the operation of one unit in the industrial/energy group (manufacture of electric power generating systems). Stip. ¶¶ 31-34, 36 (J.A. 161-63). Bendix also engaged in a variety of other less significant activities in New Jersey and sold its full range of products to customers in the State. Stip. ¶¶ 35, 37, 38 (J.A. 162-63).

## **2. Bendix's Corporate Strategies and Its History of Selective Acquisitions and Divestitures**

As is the practice with many corporations (J.A. 140-41), Bendix's management articulated corporate strategies to guide the operations of its business. Pet. App. A 3a. These strategies changed over the years. Pet. App. A 3a-4a. During the years at issue,<sup>3</sup> one of these strategies was "to diversify the company's holdings and strengthen its operations." Pet. App. A 3a.

"Bendix's strategies to pursue diversification and growth in both domestic and foreign markets" (Pet. App. A 4a) were implemented by a "careful diversification... into four broad lines of business—automotive, aerospace-electronics, industrial-energy and shelter." Pet. App. A 4a (quoting Bendix's 1975 Annual Report, Stip. ¶ 144 (J.A.

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<sup>3</sup> Bendix acquired its ASARCO stock in late 1977 and 1978. It sold the stock in 1981, triggering the gain that is at issue here.

189)).<sup>4</sup> William Agee, who was Chairman and Chief Executive Officer of Bendix from 1977 to 1983, observed in Bendix's 1977 Annual Report that "'we have pursued a deliberate policy of diversification both within and among our lines of business, and geographically as well, in an effort to arrive at a combination of activities that helps insulate the company as a whole from the ups and downs of any one of them.'" Pet. App. A 5a.

One of the ways in which Bendix pursued its corporate strategies of growth and diversification was through "selective" acquisitions and divestitures. Stip. ¶ 128 (J.A. 183). These transactions were designed to foster "corporate expansion in new areas or of existing business activities." Pet. App. 4a. During the late 1960s and 1970s, virtually all of the companies that Bendix acquired were directly related to one of its four core businesses, although Bendix occasionally acquired companies in industries in which it had no prior involvement. Stip. ¶¶ 128-165 (J.A. 183-195).

### **3. Bendix's Purchase and Sale of Its Minority Interest in ASARCO**

#### **a. Bendix's acquisition of a 20.6 percent investment in ASARCO**

In 1977, Bendix began to consider the acquisition of an interest in a company in the mining industry. Stip. ¶ 42 (J.A. 165); Stip. Exh. D (J.A. 231-33). In contrast to

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<sup>4</sup> In its annual reports from 1970-81, Bendix referred interchangeably to the "forest products" or "shelter" sectors, which under either name represented building materials, mobile homes, and manufactured homes.

Bendix's historical pattern of acquiring companies that strengthened or complemented its existing lines of business, Bendix's consideration of an investment in a mineral resource company signaled an interest in an industry with which it had no prior connection or experience and which bore no relation to its core businesses. Bendix was nevertheless attracted to the industry because Bendix believed that the industry was undervalued and had potential for significant growth in the 1980s. Stip. ¶ 44 (J.A. 165); Stip. Exh. E. (J.A. 87-118).

In late 1977, Bendix began open market purchases of stock in ASARCO and Kennecott Copper Corporation, two major copper producers. Stip. Exh. F (J.A. 128). By March 1978, Bendix's management had settled on ASARCO as its vehicle for investing in the mining industry. Stip. Exh. E (J.A. 87-118). ASARCO was one of the world's leading producers of nonferrous metals and nonmetallic minerals. It also smelted and refined nonferrous metal ores mined by others. Stip. ¶ 39 (J.A. 163-64).

On April 13, 1978, Bendix's Chairman, William Agee, sought and received approval from the Bendix Board of Directors to purchase up to 21 percent of ASARCO's stock. The decision to limit the investment to approximately 20 percent of ASARCO's stock was based on a desire to avoid investing an undue share of Bendix's assets in a business with which Bendix had no prior experience and to avoid excessive exposure to the cyclical-ity of ASARCO's earnings. Stip. Exh. F (J.A. 127-128). In this respect, as Agee subsequently testified, the decision to invest in ASARCO was "different" (J.A. 28-30), from Bendix's previous decisions to acquire companies, or interests in companies, because "[i]t was a nonoperating situation" (*id.*) and "a situation where it was a passive" investment. (J.A. 54-56).

On April 13, 1978, Bendix and ASARCO entered into a stock purchase agreement under which ASARCO agreed to sell 3,800,000 of ASARCO's shares to Bendix. Stip. ¶ 50 (J.A. 166-67). Bendix in turn agreed that prior to January 1, 1985, it would not acquire more than 21 percent of ASARCO's voting stock and that Bendix would not, either directly or through subsidiaries or affiliates, be a participant in any election contest relating to the election of ASARCO's directors. *Id.* Subsequent to the stock purchase from ASARCO, Bendix made a series of smaller purchases so that, upon completion of all purchases in November 1978 and the retirement by ASARCO of certain outstanding shares, Bendix owned 20.6 percent of ASARCO's stock. Stip. ¶ 51 (J.A. 167).

**b. The relationship between Bendix and ASARCO**

During the brief period that Bendix held its stock interest in ASARCO (1978-1981), Bendix and ASARCO remained discrete business enterprises with virtually no corporate interaction. Aside from holding the investment itself, Bendix did not engage in any business or activity in New Jersey or elsewhere that involved any business or activity in which ASARCO was engaged. Stip. ¶ 41 (J.A. 164-65). Indeed, the parties have stipulated that "[d]uring the period that Bendix held its investment in Asarco, Bendix and Asarco were unrelated business enterprises each of whose activities had nothing to do with the other." Stip. ¶ 62 (J.A. 169).

The complete absence of any functional relationship between Bendix and ASARCO was reflected in the following stipulated facts:



- There were no common management, officers, or employees of Bendix and ASARCO.
- There was no use by Bendix of ASARCO's corporate plant, offices, or facilities and no use by ASARCO of Bendix's corporate plant, offices, or facilities.
- There was no rent or lease of any property by Bendix from ASARCO and no rent or lease of any property by ASARCO from Bendix.
- Bendix and ASARCO were each responsible for providing their own legal services, contracting services, tax services, finance services and insurance.
- Bendix and ASARCO had separate personnel and hiring policies and separate pension and employee benefit plans.
- Bendix did not lend monies to ASARCO and ASARCO did not lend monies to Bendix.
- There were no joint borrowings by Bendix and ASARCO.
- Bendix did not guaranty any of ASARCO's debt and ASARCO did not guaranty any of Bendix's debt.
- ASARCO had no representatives on Bendix's Board of Directors.
- Bendix did not pledge its ASARCO stock.

- As far as can be determined, there were no sales of product by ASARCO to Bendix or by Bendix to ASARCO. There were certain sales of product in the ordinary course of business by ASARCO subsidiaries to Bendix, but these sales were minute compared to ASARCO'S total sales of \$1.7 billion in 1979 and \$1.8 billion in 1980. These sales were at arm's length prices and did not come about due to the Bendix investment in ASARCO.
- There were no transfers of employees between Bendix and ASARCO.

Stip. ¶ 62 (J.A. 169-71).

There were in fact only two limited situations in which Bendix and ASARCO had any contact at all. First, in order to account properly for Bendix's investment on the equity method,<sup>5</sup> Bendix would send two or three individuals to ASARCO's New York headquarters each fiscal quarter to gather financial information and would at times receive such information over the telephone or through the mails. Stip. ¶ 56 (J.A. 168). Second, while Bendix held the ASARCO stock, William Agee and Malcolm Baldrige, a Bendix outside director, held seats on ASARCO's 14-member Board of Directors. Consistent with this limited board presence, Bendix did not exert any control over ASARCO. Stip. ¶¶ 53, 54 (J.A. 168).

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<sup>5</sup> Because Bendix owned at least 20 percent of ASARCO's stock, Bendix accounted for this investment for financial reporting purposes under what is known as the "equity method." Under this method, Bendix included in its income its proportionate share of ASARCO's income or loss. Stip. ¶ 55 (J.A. 168).



**c. Bendix's sale of its minority interest in ASARCO**

In the fall of 1980, less than two years after the acquisition was completed, Bendix decided to sell its ASARCO stock. Stip. ¶ 63 (J.A. 171). Among the reasons for this decision were the appreciation in the stock's price and Bendix's desire to reduce its investment in businesses tied to natural resources. Stip. ¶ 64 (J.A. 171). In October 1980, Bendix and ASARCO entered into an agreement under which ASARCO agreed to purchase all of Bendix's ASARCO shares. Stip. ¶ 66 (J.A. 172). In 1981, Bendix sold its ASARCO shares to ASARCO and realized a capital gain of approximately \$211.5 million. Stip. ¶ 67 (J.A. 172).

Bendix used the proceeds from the sale for essentially two purposes: to repurchase shares of outstanding Bendix stock, and to help finance the proposed acquisition of Martin Marietta Corporation. Pet. App. A 9a. Martin Marietta's principal business was in the aerospace industry, where it was a prime contractor producing entire systems, with a strong involvement in missiles. Stip. ¶ 163 (J.A. 194). Bendix, whose aerospace group acted primarily as a subcontractor of component parts for aircraft, believed that the businesses of Bendix and Martin Marietta were complementary. *Id.* Although Bendix was able to purchase 70 percent of the stock of Martin Marietta, Bendix was unable to consummate the takeover of Martin Marietta, and Bendix was thereafter acquired by Allied Corporation. Stip. ¶ 165 (J.A. 194-95).

**4. The Tax Assessment**

New Jersey imposes its Corporation Business Tax ("CBT"), N.J. Stat. Ann. §§ 54:10A-1 *et seq.*, upon every

corporation for the privilege of exercising its corporate franchise, doing business, employing or owning capital or property, or maintaining an office in the state. *Id.* § 54:10A-2 (Pet. App. D 68a). The CBT is measured by a corporation's "entire net income," which is defined as its federal taxable income with certain adjustments not here at issue. Such income is then apportioned to New Jersey by the familiar three-factor formula of property, payroll, and sales. *Id.* §§ 54:10A-4(k), -6 (Pet. App. D 69a).

On its 1981 CBT return, Bendix excluded from its "entire net income" the gain attributable to the sale of its ASARCO stock. Bendix did so on the ground that New Jersey could not constitutionally include in Bendix's apportionable tax base income from the sale of its investment in a corporation whose business activities had nothing to do with Bendix's business activities in New Jersey.<sup>6</sup> Following an audit, the Director of the Division of Taxation determined that Bendix was not entitled to the full refund claimed on its 1981 return, based in part on his position that Bendix's gain from the sale of its ASARCO stock was taxable by New Jersey.

## 5. The Proceedings Below

The New Jersey Tax Court and the Appellate Division of the New Jersey Superior Court both cited this Court's decisions in *ASARCO Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307 (1982) and *F.W. Woolworth Co. v.*

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<sup>6</sup> Bendix also excluded capital gain income from the sale of a subsidiary, United Geophysical Corporation, and interest income that Bendix earned on the proceeds of the ASARCO and United Geophysical sales. Although both of these items were at issue in the courts below, petitioner is not pressing in this Court its claims with respect to these items.

*Taxation and Revenue Department*, 458 U.S. 354 (1982). Pet. App. C 59a n.3; Pet. App. B 30a, 31a. Indeed, the Appellate Division explicitly recognized that those decisions barred the states from taxing the income earned by a nondomiciliary corporation from its investment in another corporation if the income merely "contributes to or furthers the taxpayer's business." Pet. App. B 31a. Both New Jersey courts nevertheless rejected Bendix's constitutional objections, reasoning that Bendix's activities in managing its investment in ASARCO provided a sufficient link between New Jersey and Bendix's gain to permit New Jersey to tax the gain. The Appellate Division acknowledged, however, that "*Asarco* and *F.W. Woolworth* cast a dark shadow over the Tax Court's decision...." Pet. App. B 32a.

The New Jersey Supreme Court affirmed. Pet. App. A 24a. It recognized that, in order to tax an apportioned share of the income earned by a nondomiciliary corporation conducting a multistate business within the state, the state must have a minimum connection with the activities that generate such income. That minimum connection, the court further recognized, exists when the income in question is derived from a unitary business conducted both within and without the state. "The unitary business principle, characterized as the 'linchpin of apportionability,' provides the foundation to satisfy due process and commerce clause restraints." Pet. App. A 12a (quoting *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 439 (1980)).

In addressing the question whether Bendix's income from its investment in ASARCO was derived from a unitary business carried on in New Jersey, however, the state court did not focus on the relationship of the underlying activities of the two enterprises, as this Court has in

its unitary business opinions. See *Mobil*; *ASARCO*; *Woolworth*. Indeed, the court took no exception to the parties' stipulation that Bendix and ASARCO "were unrelated business enterprises each of whose activities had nothing to do with the other." Stip. ¶ 62 (J.A. 169).

Rejecting the accepted view that "[t]he tests for determining a unitary business are... controlled... by the relationship between the taxpayer recipient and the affiliate generator of the income that becomes the subject of State tax," the court instead focused on "the intangible nature of corporate operations... to determine the existence of a unitary business." Pet. App. A 18a. The New Jersey court looked to Bendix's broad statements concerning its investment strategies to find that Bendix had an "ingrained policy of acquisitions and divestitures" which "projected the existence of a unitary business." Pet. App. A 21a. The New Jersey court similarly concluded that Bendix "had a business function of corporate acquisitions and divestitures that was an integral operational activity." Pet. App. A 18a-19a.

The New Jersey court was evidently concerned that such investment activity might not establish the requisite link with a unitary business operation of Bendix carried on partly in New Jersey. The court attempted to establish this link by looking beyond the relationship between Bendix's investment activity and Bendix's investment in ASARCO to the use that Bendix made of the proceeds from the sale of its ASARCO stock. The proceeds were used, in part, to acquire stock in Martin Marietta Corporation, and "the purpose of acquiring Martin Marietta was to complement the aerospace-electronics facets of Bendix['s] business, some of which are located in New Jersey." Pet. App. A 20a. According to the New Jersey Supreme Court, this intangible "flow of value" be-

tween the ASARCO investment and Bendix's New Jersey operations helped meet this Court's unitary business standard articulated in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159 (1983). Pet. App. A 20a-21a.

Finally, the New Jersey Supreme Court found that this Court's decisions in *ASARCO* and *Woolworth* were distinguishable because, in the *ASARCO* case, ASARCO's stock investments were "'not integral to nor a necessary part of [ASARCO's] business operation'" (Pet. App. A 21a), and because ASARCO did not use "'its stock as security for borrowing of working capital [to] acquire stock or securities in other companies.'" *Id.* The New Jersey Supreme Court also commented that "neither *ASARCO* nor *F.W. Woolworth* involved the purchase of 4,000,000 shares of outstanding corporate stock to enhance the stockholder value of the corporation." Pet. App. A 21a.

### SUMMARY OF ARGUMENT

A. Under the Commerce and Due Process Clauses, a state does not have the power to tax a person, property or transaction unless there is a definite link or minimum connection between the state and the person, property or transaction. In the context of state corporate income tax apportionment, this nexus requirement is reflected in the unitary business principle. When a multi-state enterprise conducts a unitary business within and without a state, the state has the requisite nexus to both the in-state and out-of-state activities of the business to include all of the income generated by these activities in the taxpayer's apportionable tax base. When a nondomiciliary taxpayer's activities carried on within the state are not unitary with activities carried on outside the state, however, the state may not include the income from



those out-of-state activities in the taxpayer's apportionable tax base.

In a series of decisions in the early 1980s,<sup>7</sup> this Court defined a unitary business as one characterized by functional integration, centralization of management, and economies of scale. Applying this standard to cases involving the power of a state to tax income earned by nondomiciliary corporations from their investments in other corporations, this Court held that the apportionability of the income depended on whether it was earned in the course of activities related in some concrete way to the taxpayer's business activity in the taxing state.

B. The relationship between Bendix and ASARCO did not provide the constitutionally required nexus to justify New Jersey's inclusion in Bendix's apportionable tax base of Bendix's income from its investment in ASARCO. The undisputed facts show that Bendix and ASARCO were not engaged in a unitary business. Hence the "linchpin of apportionability" (*Mobil*, 445 U.S. at 439) was absent.

C. The court below reasoned that Bendix's investment in ASARCO was part of Bendix's unitary business because (i) Bendix had a long-term corporate strategy of acquisitions and divestitures to expand and diversify its business and (ii) Bendix's purchase and sale of ASARCO fell within this "operational" strategy. In *ASARCO* and *Woolworth*, however, this Court considered and rejected a unitary business theory identical in all

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<sup>7</sup> *Mobil*; *Exxon Corp. v. Wisconsin Dep't of Revenue*, 447 U.S. 207 (1980); *ASARCO*; *Woolworth*; *Container*.

essential respects to the theory advanced by the court below. This Court unequivocally repudiated such a definition of a unitary business based on "corporate purpose," *ASARCO*, 458 U.S. at 326 (emphasis in original), observing that it would "destroy the concept," *id.*, and "trivialize this due process limitation." *Woolworth*, 458 U.S. at 363.

While the analysis by the court below was couched in terms of Bendix's "ingrained acquisition-divestiture policy," which that court characterized as amounting to "integral operational activity" (Pet. App. A 18a-19a), this is simply another way of describing Bendix's business purpose for making an investment. Attaching the label "integral operational" to capital investment activities does not change their essential character. Whatever "policy" may have driven Bendix's investment in *ASARCO*, it was a passive investment: Bendix did not control and was not functionally integrated with *ASARCO*. In this respect, a comparison of the actual relationship between Bendix, *ASARCO*, and *Woolworth* and their respective investments reveals that Bendix's investment in *ASARCO* was even less eligible to be classified as unitary than the investments the Court found non-unitary in *ASARCO* and *Woolworth*.

Furthermore, the decision below makes the apportionability of investment income turn upon the vagaries of the investment's relationship to the corporation's strategy rather than upon the investment's relationship in some concrete way to the taxpayer's in-state activities. It thereby erases the sharp line that this Court has drawn between investments that have a definite link or connection to the taxpayer's business activities in the taxing state and those that merely serve the function of diversifying the corporate portfolio.



D. This Court's decision in *Container*, which expressly reaffirmed *ASARCO* and *Woolworth*, reinforces the conclusion that New Jersey lacks the requisite nexus with Bendix's investment in *ASARCO* to permit New Jersey to tax Bendix's gain from the sale of its *ASARCO* stock.

E. Allowing the decision below to stand would undermine the doctrine of *stare decisis*. It would also remove meaningful limitations on the states' power to tax the investment income of multistate corporations, exposing such income to taxation by any state in which the corporation did business, regardless of the connection between the taxpayer's investment and its activities in the taxing state. And it would erode the principles of fairness and constitutional restraint on which this Court's unitary business principles are so soundly based.

## ARGUMENT

**UNDER THE COMMERCE AND DUE PROCESS CLAUSES, NEW JERSEY MAY NOT TAX BENDIX'S INCOME FROM THE SALE OF BENDIX'S MINORITY INVESTMENT IN ASARCO BECAUSE THERE WAS NO "DEFINITE LINK" OR "MINIMUM CONNECTION" BETWEEN BENDIX'S ACTIVITIES IN NEW JERSEY AND BENDIX'S INVESTMENT IN ASARCO**

- A. **"The Linchpin of Apportionability in the Field of State Income Taxation Is the Unitary-Business Principle."**

A fundamental limitation on the states' power to

tax—a limitation arising out of both the Due Process and Commerce Clauses—is that there be “some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.” *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954). When such a “substantial nexus” (*Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977)) exists, a state may properly demand a return for the “protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society.” *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940). When no substantial nexus exists, however, the state has not “given anything for which it can ask return.” *Id.*

In the context of state corporate income taxation, the nexus requirement is reflected in the unitary business principle, which confines the states’ power to include income from out-of-state activities in the taxpayer’s apportionable tax base. If a taxpayer is carrying on a single “unitary” business within and without the state, the state has the requisite nexus to both the in-state and out-of-state activities of the business to justify the state’s inclusion of all of the income generated by these activities in the taxpayer’s apportionable tax base. By the same token, however, when the activities carried on within the state are not unitary with the activities carried on elsewhere, the state is constitutionally constrained from including the income arising from those out-of-state activities in the taxpayer’s apportionable tax base, at least when the taxpayer is not domiciled in the taxing state.

In a series of decisions handed down during the early 1980s,<sup>8</sup> this Court delineated the contours of the unitary business principle as applied to state corporate income taxes imposed upon nondomiciliary taxpayers.<sup>9</sup> In *Mobil*, Vermont sought to include in Mobil's appor-

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<sup>8</sup> *Mobil*; *Exxon*; *ASARCO*; *Woolworth*; *Container*.

<sup>9</sup> The unitary business principle itself is a venerable one. It derives from the "unit rule" developed in the late nineteenth century for apportioning property values of interstate railroad, telegraph, and express companies to state and local taxing jurisdictions. See, e.g., *State R.R. Tax Cases*, 92 U.S. 575, 608 (1875) ("It may well be doubted whether any better mode of determining the value of that portion of the track within any one county has been devised than to ascertain the value of the whole road, and apportion the value within the county by its relative length to the whole"); *Adams Express Co. v. Ohio*, 165 U.S. 194, 222 (1897) ("[W]hile the unity which exists may not be a physical unity, it is something more than a mere unity of ownership. It is a unity of use, not simply for the convenience or pecuniary profit of the owner, but existing in the very necessities of the case—resulting from the very nature of the business").

None of the state corporate income tax cases reaching the Court prior to 1980 undertook a detailed exploration into the scope of the unitary business doctrine. This was very likely attributable to the fact that the taxpayers in those cases, who were typically engaged in manufacturing and mercantile activity, were indisputably carrying on a unitary business within and without the taxing state. See *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920); *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n*, 266 U.S. 271, 282 (1924) ("the Company carried on the unitary business of manufacturing and selling ale"); *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123, 133 (1931) ("the enterprise of a corporation which manufactures and sells its manufactured product is ordinarily a unitary business"); *Butler Bros. v. McCollgan*, 315 U.S. 501, 508 (1942) (taxpayer's business is "unitary... [t]here is unity of ownership and management. And the operation of the central buying division alone demonstrates that functionally the various branches are closely integrated") (citation omitted); *General Motors Corp. v. District of Columbia*, 380 U.S. 553 (1965); *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978).

tionable tax base dividends that Mobil received from its foreign subsidiaries engaged in the oil and gas business. Articulating the controlling doctrine, this Court declared that "the linchpin of apportionability in the field of state income taxation is the unitary-business principle." 445 U.S. at 439. The Court described a unitary business as one characterized by "functional integration, centralization of management, and economies of scale." *Id.* at 438. Since Mobil was engaged in a functionally integrated, centrally managed business extending from oil wells in foreign countries to gas pumps in Vermont, it followed that Vermont had the requisite nexus with Mobil's out-of-state activities to include income from such activities in Mobil's apportionable tax base. The fact that the income was received in the form of dividends, reflecting profits from such activities, rather than direct operating income, was of no constitutional significance. *Id.* at 440-41. Mobil had failed to prove that its dividend income was "earned in the course of activities unrelated to" its business activity in the taxing state. *Id.* at 439. *Exxon*, which followed on *Mobil's* heels, was to the same effect.<sup>10</sup>

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<sup>10</sup> *Exxon* reiterated that "[t]he 'linchpin of apportionability' for state income taxation of an interstate enterprise is the 'unitary-business principle.'" 447 U.S. at 223 (quoting *Mobil*, 445 U.S. at 439). It focused on the question whether Exxon's petroleum marketing activities carried on in Wisconsin were related to its refining and production activities carried on elsewhere to justify including the income from all such activities in Exxon's apportionable tax base. Determining that the case "involves a highly integrated business" (*id.* at 224) characterized by internal transfers of raw materials (*id.* at 226), centralized purchasing (*id.* at 224), and interdepartmental coordination (*id.*), the Court concluded that Exxon's production, refining, and marketing operations constituted a unitary business. Consequently, Wisconsin had the requisite nexus with the rest of Exxon's activities to include income from such activities in Exxon's apportionable tax base.

ASARCO involved the question whether Idaho could include within a nondomiciliary corporation's apportionable tax base intangible income (dividends, interest, and capital gains) that the corporation had derived from its investment in subsidiaries. As in *Mobil* and *Exxon*, the answer to that question depended on whether the income derived from the taxpayer's unitary business being carried on within and without the taxing state. ASARCO's relationship to its subsidiaries did not reveal the functional integration, centralization of management, or economies of scale that are essential to the existence of a unitary business. *ASARCO*, 458 U.S. at 320-24. Because the subsidiaries were "discrete business enterprises" (*ASARCO*, 458 U.S. at 320, quoting *Exxon*, 447 U.S. at 224), this Court was satisfied that there was no "minimum connection" between ASARCO's business activities in Idaho and the activities of ASARCO's subsidiaries. Consequently, this Court held there was no constitutional predicate for sweeping income from ASARCO's investments in its subsidiaries into its Idaho apportionable tax base.

*Woolworth*, a companion case to *ASARCO*, reiterated and reinforced *ASARCO*'s teachings. This Court held that New Mexico could not include in a New York-based retailer's apportionable tax base intangible income that the retailer derived from its subsidiaries, because the subsidiaries operated "discrete business enterprise[s]" (*Woolworth*, 458 U.S. at 372) and "a 'showing has been made that income unconnected with the unitary business has been used in the' levy of the New Mexico tax." *Id.* (quoting *Butler Bros. v. McColgan*, 315 U.S. 501, 509 (1942)).

In *Container*, this Court revisited the unitary business question in the context of a worldwide paperboard



manufacturing business operated by the taxpayer and its foreign subsidiaries. Noting that the unitary business principle was now "well-established," 463 U.S. at 176, the Court emphasized the requirement that the apportionability of income derived from "the out-of-state activities of the purported 'unitary business' be related in some concrete way to the instate activities." *Id.* at 166. The Court continued:

The functional meaning of this requirement is that there be some sharing or exchange of value not capable of precise identification or measurement—beyond the mere flow of funds arising out of a passive investment or a distinct business operation.

*Id.* Under these standards, the Court found that the taxpayer and its subsidiaries were engaged in a unitary business in light of the taxpayer's assistance to its subsidiaries in obtaining equipment, filling personnel needs, making and guaranteeing loans, and providing technical aid. *Id.* at 179-80. The Court easily distinguished *ASARCO* and *Woolworth* as cases not involving "a 'functionally integrated enterprise'... which the State is entitled to tax as a single entity." *Id.* at 179 (citation omitted).

*Mobil, Exxon, ASARCO, Woolworth, and Container* thus establish the broad principles for determining whether a unitary link exists between a nondomiciliary taxpayer's business activities within the state and its investment in another corporation. Such a link must be found before a state may constitutionally include income from such investment in the taxpayer's apportionable tax base. But as we demonstrate in the succeeding sections of

this brief, no such unitary link existed between Bendix's activities in New Jersey and its investment in ASARCO.

**B. Bendix's Relationship to ASARCO Did Not Provide the "Definite Link" or "Minimum Connection" Between Bendix's Activities in New Jersey and Bendix's Investment in ASARCO That Would Permit New Jersey to Tax Bendix's Income from the Sale of Its Minority Investment in ASARCO**

There can be no serious claim in this case that the business relationship between Bendix and ASARCO provided a constitutionally sufficient predicate for inclusion in Bendix's apportionable tax base of its income from its investment in ASARCO.<sup>11</sup> The undisputed facts show that "[d]uring the period that Bendix held its investment in Asarco, Bendix and Asarco were unrelated enterprises each of whose activities had nothing to do with the other." Stip. ¶ 62 (J.A. 169); see pp. 7-9, *supra*. Moreover, the record does not contain anything that could remotely be read to suggest that the relationship between Bendix and ASARCO was characterized by the unitary attributes of functional integration, centralized management, or economies of scale. The conclusion is inescapable that Bendix and ASARCO remained "discrete business enterprise[s]" (*Exxon*, 447 U.S. at 224) and did not conduct a unitary business. Their relationship therefore fails to provide the "minimum connection" between Bendix's New Jersey business activities and its

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<sup>11</sup> Implicitly recognizing this point, the New Jersey Supreme Court did not rest its decision on this ground. Pet. App. A 18a-22a. See Subsection C, *infra*.



minority investment in ASARCO that would justify the inclusion in Bendix's apportionable tax base of its income from its investment in ASARCO. See *Mobil*; *Exxon*; *ASARCO*; *Woolworth*; *Container*.

**C. Bendix's Statements of Corporate Strategy Did Not Forge the "Definite Link" or "Minimum Connection" Between Bendix's Activities in New Jersey and Bendix's Investment in ASARCO That Would Permit New Jersey to Tax Bendix's Income From the Sale of Its Minority Investment in ASARCO**

Because the functional relationship between Bendix and ASARCO wholly failed to provide a unitary link between Bendix's activities in New Jersey and its investment in ASARCO, the court below was compelled to look elsewhere in its effort to fashion such a link. In so doing, the court looked to the investment relationship between Bendix and its ASARCO stock. According to the New Jersey Supreme Court, "[w]hen capital investment activities are long-term integral operational corporate functions rather than passive investment functions, they can serve as the basis for concluding a unitary business exists." Pet. App. A 19a. Because Bendix, in the court's view, "essentially had a business function of corporate acquisitions and divestitures that was an integral operational activity" *id.* at 18a-19a, and because Bendix's investment in ASARCO, according to the court, was a part of this activity, the court claimed that it followed that Bendix's investment in ASARCO was part of Bendix's unitary "integral operational" capital investment business. Under this theory, New Jersey enjoyed the requisite unitary link with Bendix's investment in ASARCO because there was a "flow of value" generated in part by

subsequent use of proceeds of the sale of the ASARCO stock to help finance Bendix's unsuccessful takeover attempt of Martin Marietta, whose operations would have complemented Bendix's New Jersey aerospace business. Pet. App. A 20a-21a. Upon examination, however, the New Jersey Supreme Court's theory collapses.

**1. The New Jersey Opinion Is a Semantic End Run Around This Court's ASARCO and Woolworth Decisions**

In *ASARCO* and *Woolworth*, this Court considered and rejected a unitary business theory identical in all essential respects to the theory advanced by the New Jersey court. Despite the absence of a unitary link between the underlying activities of ASARCO and Woolworth and their respective subsidiaries (see p. 21, *supra*), Idaho and New Mexico contended in *ASARCO* and *Woolworth* that a unitary link nevertheless existed.

Idaho argued that "intangible income should be considered a part of a unitary business if the intangible property (the shares of stock) is 'acquired, managed or disposed of for purposes relating or contributing to the taxpayer's business.'" *ASARCO*, 458 U.S. at 326 (quoting Brief for Appellee 4). Idaho likewise urged "that income from intangible property be considered part of a unitary business when the intangibles 'contribute to or relate to or are [in] some way in furtherance of the taxpayer's own trade or business.'" *Id.* (quoting Tr. of Oral Arg. 25). Idaho further asserted that "[i]t is this integration—i.e., between the business use of the intangible asset (the shares of stock) and ASARCO's mining, smelting, and refining business—which makes the income part of the unitary business." *Id.* (quoting Brief for Appellee 4).

This Court unequivocally repudiated this concept of a unitary business based on the purported unitary links between a corporation's investment objectives and its operations:

This definition of unitary business would destroy the concept. The business of a corporation requires that it earn money to continue operations and to provide a return on its invested capital. Consequently *all* of its operations, including any investment made, in some sense can be said to be "for purposes related to or contributing to the [corporation's] business." When pressed to its logical limit, this conception of the "unitary business" limitation becomes no limitation at all. When less ambitious interpretations are employed, the result is simply arbitrary.

ASARCO, 458 U.S. at 326 (footnote omitted).

New Mexico, like Idaho, argued that the taxpayer's income from its investments in its subsidiaries was taxable because the investments were "motivated by business considerations" (Brief for Appellee at 16, *Woolworth*) and were an "integral part" of the taxpayer's business. *Id.* at 18. New Mexico also contended that the investments could be considered part of the taxpayer's unitary business because, as the state court had reasoned:

"The possession of large assets by subsidiaries is a business advantage of great value to the parent; 'it may give credit which will result in more economical business methods; it may give a standing which shall facilitate purchases; it may enable the corporation to enlarge the field of its activities and in many ways give it business standing and pres-

tige.' *Flint v. Stone Tracy Co.*, 220 U.S. 107, 166 ... (1911)." 95 N.M., at 529, 624 P.2d, at 38.

*Woolworth*, 458 U.S. at 363 (quoting the New Mexico court).

As it had done in *ASARCO*, this Court again squarely rejected the notion that income from a non-domiciliary taxpayer's investments was part of a taxpayer's unitary business merely because the investment advanced the taxpayer's business purposes:

The state court's reasoning would trivialize this due process limitation by holding it satisfied if the income in question 'adds to the riches of the corporation....' Income, from whatever source, always is a 'business advantage' to a corporation. Our cases demand more. In particular, they specify that the proper inquiry looks to 'the underlying unity or diversity of business enterprise,' not to whether the nondomiciliary parent derives some economic benefit—as it virtually always will—from its ownership of stock in another corporation.

*Woolworth*, 458 U.S. at 363-64 (citations and footnote omitted).<sup>12</sup>

The New Jersey Supreme Court's unitary analysis may differ somewhat in form, but it does not differ in substance, from the discredited unitary theories advanced by the states in *ASARCO* and *Woolworth*. In each case, the state took the position that a nondomiciliary corporate taxpayer's income from an investment in another corporation should be includible in the taxpayer's apportionable tax base even if the underlying activities of the two corporations are not unitary. In each case, the grounds claimed for including such income in the tax-

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<sup>12</sup> Most state courts have faithfully adhered to the teachings of *ASARCO* and *Woolworth* and have recognized that they preclude apportionment of capital gain from the sale of non-unitary subsidiaries. *Super Valu Stores, Inc. v. Iowa Dep't of Revenue and Finance*, No. 320/90-1557 (S. Ct. Iowa Dec. 24, 1991); *Pledger v. Illinois Tool Works, Inc.*, 306 Ark. 134, 812 S.W.2d 101, cert. denied, 112 S. Ct. 418 (1991); *Corning Glass Works, Inc. v. Virginia Dep't of Taxation*, 241 Va. 353, 402 S.E.2d 35, cert. denied, 112 S. Ct. 277 (1991); *James v. International Tel. & Tel. Corp.*, 654 S.W.2d 865 (Mo. 1983) (*en banc*); cf. *Brunner Enter., Inc. v. Department of Revenue*, 452 So. 2d 550 (Fla. 1984). Indeed, even where state courts have held that, in some circumstances, a taxpayer's income is apportionable when derived from an investment where the payor is not unitary with the payee, virtually all of them have done so on the ground that the income from the investments was essential to the operation of the taxpayer's own unitary business. *American Home Products Corp. v. Limbach*, 49 Ohio St. 3d 158, 160-162, 551 N.E.2d 201, 204-205, cert. denied, 111 S. Ct. 63 (1990); *NCR Corp. v. Comptroller*, 313 Md. 118, 133-41, 544 A.2d 764, 771-75 (1988); *Lone Star Steel Co. v. Dolan*, 668 P.2d 916, 924-25 (Colo. 1983). No such claim could be made in this case. Stip. ¶ 62 (J.A. 169-171); see pp. 38-40, *infra*. Nevertheless, the amicus brief filed on behalf of 20 states in support of Virginia's unsuccessful petition for certiorari in the *Corning Glass Works* case, *supra*, makes a solid showing of the contemporary overzealousness with which the taxing authorities in some states are seeking substantial new sources of revenue without regard to the constitutional limitations applicable here.



payer's apportionable tax base were that the investment *qua* investment was related to the taxpayer's activities in the taxing state. And in each case, the alleged "unitary" link between the investment and the taxpayer's activities in the taxing state was the taxpayer's business purpose.

To be sure, the phrasing of the New Jersey court's analysis was more embellished than the analysis proffered by the states in the *ASARCO* and *Woolworth* cases. Rather than relying on the naked "business purpose" of the investment as creating a unitary link between the taxpayers' business activities in the state and their investment, the New Jersey court found such a link in Bendix's "ingrained acquisition-divestiture policy designed to expand and enhance its existing operations as well as to move it into other fields of business." Pet. App. A 18a. According to the New Jersey court, capital investment activities can serve as the basis for concluding a unitary business exists, when they are "long-term integral operational corporate functions" (Pet. App. A 19a), or constitute "integral operational activity." *Id.*

But attaching the label "integral operational" to capital investment activities does not change their character. There is no blinking the fact that, whatever the "purpose" or "policy" underlying Bendix's investment in *ASARCO*, it was a passive investment; Bendix did not control and was not functionally integrated with *ASARCO*. Stip. ¶¶ 41, 54 (J.A. 164-65, 168). In these respects, Bendix's investment in *ASARCO* was indistinguishable from the investments the Court found non-unitary in *ASARCO* and *Woolworth*. The assumption that Bendix's investment in *ASARCO* might have been motivated by Bendix's strategy of growth and diversification (see pp. 4-5, *supra*), or indeed, by an "ingrained policy of acquisitions and divestitures" (Pet. App. A 21a) does not



make the investment unitary any more than ASARCO's and Woolworth's corporate purposes for acquiring their investments made their respective investments unitary.

This is not to suggest that many, if not most, of Bendix's investments in corporations and other assets were not in fact part of its unitary business. These were acquisitions of operating companies and the assets of companies that fell squarely within Bendix's four core business groups and which enhanced Bendix's existing product areas.<sup>13</sup> See pp. 3-5, *supra*; Stip. ¶¶ 128-165 (J.A. 183-95). The reason that these investments were part of Bendix's unitary business, however, was not because they were made pursuant to some "long-term planning strategy" or an "ingrained acquisition-divestiture policy." Pet. App. A 18a. It was because they were related to

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<sup>13</sup> For example, during the late 1960s and 1970s, Bendix acquired P & D Manufacturing Company, a manufacturer of automotive ignition parts, Stip. ¶ 132 (J.A. 185), Fram Corporation, a manufacturer of automotive oil and air filters, Stip. ¶ 133 (J.A. 185), and the Autolite spark plug manufacturing facility and the Autolite trademark. Stip. ¶ 142 (J.A. 188). These acquisitions extended Bendix's reach into the automotive industry, particularly in the automobile "after market." Stip. ¶ 128 (J.A. 183). During the late 1960s, Bendix acquired Besly-Welles, a manufacturer of grinding machines and metal cutting tools, Stip. ¶ 132 (J.A. 185), Titan Abrasives Company, a manufacturer of abrasive grinding disks for the cutting tool industry, Stip. ¶ 133 (J.A. 185), and American Abrasive Company, a manufacturer of abrasive grains, powders, and wheels. Stip. ¶ 137 (J.A. 187). These acquisitions furthered Bendix's involvement in the industrial/energy sector. During the 1970s, Bendix acquired Bass & Co., a retailer of specialty building materials, Caradco, a manufacturer of wood windows and doors, Modern Materials, a producer of aluminum building products, and Coin Millwork, a maker of moldings. Stip. ¶ 129 (J.A. 184). All of these companies used forest products as raw materials, and their acquisition was a natural extension of Bendix's forest products business. *Id.*

Bendix's business through centralization of management, functional integration, and economies of scale. Indeed, these investments would have been part of Bendix's unitary business even if there had been no strategy behind their acquisition. It is not the purpose or strategy behind a corporate investment that makes it unitary; it is the functional relationship of the corporation to the investment that is critical.

**2. The Relationship Between ASARCO and Woolworth and Their Investments in Their Respective Subsidiaries Was Much Closer Than the Relationship Between Bendix and Its Minority Investment in ASARCO**

A comparison of the relationship between Bendix, ASARCO, and Woolworth and their respective investment demonstrates that Bendix had a more attenuated relationship to its investment in ASARCO than either ASARCO or Woolworth had to their investments in their respective subsidiaries. Since this Court has held that the relationship of ASARCO and Woolworth to their subsidiaries is non-unitary from both a functional and an investment perspective, Bendix's investment in ASARCO cannot be characterized as unitary unless the holdings of ASARCO and Woolworth are to be abandoned.

As the facts summarized in the Appendix to this brief confirm, the conclusion is inescapable that ASARCO and Woolworth presented considerably stronger cases for arguing that the taxpayer's investments were part of the taxpayer's unitary business than does the instant controversy. ASARCO's investments were in companies in ASARCO's own line of business, that dealt with ASARCO as a customer and a significant supplier of raw

materials to ASARCO's business, and that, in some cases, were majority-owned by ASARCO. Woolworth's investments were in companies that were in Woolworth's own line of business, that were wholly-owned or majority-owned by Woolworth, and that Woolworth had the potential to control and did control with respect to major financial decisions. By way of contrast, Bendix's investment was in a company in a completely unrelated line of business, that had no operational dealings with Bendix, that was only 20.6 percent owned by Bendix, and that Bendix had no potential to control. However one views the strength of the states' unitary arguments in *ASARCO* and *Woolworth*—and this Court was satisfied that the arguments were insufficient—it is simply not possible to conclude on the basis of these facts that Bendix's investment in ASARCO was more "unitary" with its business than were ASARCO's and Woolworth's investments with their businesses.

Indeed, the strained attempt of the court below to paint *ASARCO* and *Woolworth* as "factually distinguishable," Pet. App. A 21a, serves only to reinforce the conclusion that the instant case has a much weaker basis for a unitary determination than did *ASARCO* and *Woolworth*. The court declares that "ASARCO's stock investments were 'not integral to nor a necessary part of [ASARCO's] business operation.'" Pet. App. A 21a (quoting *ASARCO*, 458 U.S. at 324-25 n.21, quoting the Idaho trial court). But the court utterly fails to explain how Bendix's investment in ASARCO was more "integral" to Bendix's business operations than ASARCO's investments in ASARCO were integral to ASARCO's business operations. In light of the facts of both cases (see Appendix, *infra*), the court's inability to come up with such an explanation is understandable. Moreover, the New Jersey court's observation that, in

ASARCO, ASARCO did not use "its stock as security for borrowing of working capital [to] acquir[e] stock or securities in other companies," *id.*, hardly distinguishes ASARCO from the present case; Bendix did not pledge its ASARCO stock, there were no intercompany loans, no joint borrowings, and no intercompany guarantees. Stip. ¶ 62 (J.A. 170).

Finally, the court's comment that "neither ASARCO nor *F.W. Woolworth* involved the purchase of 4,000,000 shares of outstanding corporate stock to enhance the stockholder value in the corporation" (Pet. App. A 21a) provides the most telling sign that the court has ignored the teachings of ASARCO and *Woolworth* by embracing the rejected view that "corporate purpose should define unitary business." ASARCO, 458 U.S. at 326 (emphasis in original). If the use of the proceeds from the sale of an investment "to enhance the stockholder value in the corporation" (Pet. App. A 21a) makes the investment "unitary," then the point would truly be reached at which "the 'unitary business' limitation becomes no limitation at all." ASARCO, 458 U.S. at 326. In sum, the court below has put forth a ruling which—as this Court recently said in another context, *Hunter v. Bryant*, No. 90-1440, decided December 16, 1991, 60

U.S.L.W. 3432—"ignores the import of these decisions."<sup>14</sup>

**3. The New Jersey Court's Theory That Long-Term Investment Activities "Projec[t] the Existence of a Unitary Business" When They "Have as Their Goal the Growth and Expansion of Existing Corporate Business Activities" Eviscerates the Unitary Business Concept**

When this Court rejected the notion that the corporate purpose for which an investment is held can provide the "linchpin of apportionability" (*Mobil*, 445 U.S. at 439), it sought to inter the genre of unitary analysis that the New Jersey Supreme Court is seeking to resurrect. This Court has recognized that, before a state may tax a nondomiciliary taxpayer's income from its investments, the Due Process and Commerce Clauses demand a more concrete connection between a taxpayer's in-state activities and the investments than the fact that the investments "contribute to or relate to or are in some way in furtherance of the taxpayer's own unitary business." *ASARCO*, 458 U.S. at 326 (quoting Tr. of Oral Arg. 25).

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<sup>14</sup> In addition to its unequivocal rejection of the New Jersey court's theory in *ASARCO*, this Court in *Woolworth* made a similar point in dismissing the significance that the New Mexico tribunals had attached to the fact that Woolworth had commingled its dividends with its general funds and used them "for general corporate operating purposes." *Woolworth*, 458 U.S. at 364 n.11. "This analysis likewise subverts the unitary-business limitation. All dividend income—irrespective of whether it is generated by a 'discrete business enterprise,' *Mobil*, 445 U.S. at 439—would become part of a unitary business if the test were whether the corporation commingled dividends from other corporations, whether subsidiaries or not." *Id.* (emphasis in original).



The Court thus repudiated a unitary business doctrine constructed on the broad statements of corporate strategy that emanate on a regular basis from corporate board rooms across the country and that fill the pages of annual corporate reports.

If the New Jersey Supreme Court's decision were allowed to stand, however, it would establish a unitary business doctrine largely defined by corporate rhetoric rather than by operational functions. The court's opinion purports to identify a discrete "business function" (Pet. App. A 18a) of "capital investment activities" (Pet. App. A 19a) that "become an integral part of a corporation's business." *Id.* But what distinguishes capital investment activities that are "long-term integral operational corporate functions" (Pet. App. A 19a), from those that are merely "passive investment functions" (*id.*)? The answer, according to the New Jersey court's analysis, is to be found in corporate strategy, as articulated in annual reports, memoranda, and other indicia of corporate policy. Pet. App. A 3a-6a. But from the standpoint of the fundamental question whether there is a "definite link" or "minimum connection" between Bendix's unitary business activities conducted in part in New Jersey and its investment in ASARCO, it makes no difference whether Bendix's investment in ASARCO was pursuant to an "ingrained acquisition-divestiture" strategy, Pet. App. A 18a, a strategy of "growth and diversification for the 80's," Stip. Exh. E (J.A. 87), or no strategy at all. Unless Bendix's investment in ASARCO relates "in some concrete way to the in-state activities... beyond the mere flow of funds arising out of a passive investment or a distinct business operation," *Container*, 463 U.S. at 166, the essential unitary link has not been forged. Corporate rhetoric alone cannot provide the requisite nexus.



The New Jersey court recognized this problem. Pet. App. A 20a-21a. It attempted to buttress its conclusion by looking beyond the relationship of Bendix's investment in ASARCO itself to the use that Bendix made of the proceeds from the sale of its ASARCO stock, when Bendix no longer had any connection whatsoever with ASARCO. The court noted that the proceeds were used to acquire Martin Marietta stock, and "the purpose of acquiring Martin Marietta was to complement the aerospace-electronics facets of Bendix['s] business, some of which are located in New Jersey." Pet. App. A 20a. But if the use of proceeds from an investment, *after the taxpayer has disposed of all of its interest in the investment*, can establish a due process link between the investment and the state in which the proceeds are subsequently invested, the due process limitations on state taxation have not merely been "trivialize[d]," *Woolworth*, 458 U.S. at 363, they have been obliterated.<sup>15</sup>

**D. This Court's Decision in *Container* Reinforces the Conclusion That There Was No "Definite Link" or "Minimum Connection" Between Bendix's Activities in New Jersey and Bendix's Investment in ASARCO That Would Permit New Jersey to Tax Bendix's Income From Its Investment in ASARCO**

Just one year after the Court handed down its 1982

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<sup>15</sup> This Court has discredited the theory underlying the New Jersey court's analysis—that the subsequent use of proceeds for business purposes can provide the answer to the unitary business inquiry. The Court declared that such an approach "subverts the unitary-business limitation." *Woolworth*, 458 U.S. at 364 n.11. See note 14, *supra*.

decisions in *ASARCO* and *Woolworth*, it decided *Container*. *Container* raised the question whether a domestic paperboard manufacturer was carrying on a unitary business with its foreign subsidiaries, which were engaged in the same line of business as their parent. The relationship between the taxpayer and its subsidiaries in certain respects "was decidedly close." *Container*, 463 U.S. at 173. The taxpayer played a substantial role in lending funds to the subsidiaries and in guaranteeing loans provided by others; it provided advice and consultation regarding manufacturing techniques, engineering, design, architecture, insurance, and cost accounting; it assisted its subsidiaries in their procurement of equipment and in filling personnel needs; it played a supervisory role in providing general assistance to the subsidiaries; and there was a spillover of good will between the taxpayer and its subsidiaries and considerable interplay in the area of corporate expansion. *Id.* at 173, 179. Without determining whether any one of these factors would suffice by itself to prove the existence of a unitary business, the Court held that in combination they clearly demonstrated the reasonableness of the state court's conclusion that a unitary business existed. *Id.* at 179-80.

After advertent to the factors that made *Container* and its subsidiaries unitary, the Court was careful to note that "[i]n each of these respects, this case differs from *ASARCO* and *F.W. Woolworth*, and clearly comes closer than those cases did to presenting a 'functionally integrated enterprise,' *Mobil*, [445 U.S.] at 440, which the State is entitled to tax as a single entity." 463 U.S. at 179 (footnote omitted). The Court went on to point out that in *Woolworth* no phase of any subsidiary's business was integrated with the parent's, each subsidiary made business decisions independently of the parent, each subsidiary was responsible for obtaining financing from

sources other than the parent, and there were virtually no exchanges of employees between the subsidiaries and the parent. *Id.* at n.18. In light of the fact that Bendix's relationship to ASARCO was even more attenuated than ASARCO's and Woolworth's relationships to their subsidiaries, see Appendix, *infra*, it is plain that *Container*, by reaffirming the line between cases like ASARCO and Woolworth, on the one hand, and Mobil and Exxon, on the other, has likewise reinforced the conclusion that Bendix's minority investment in ASARCO cannot be characterized as part of Bendix's unitary business.

Furthermore, this Court in *Container* affirmed its repudiation of the unitary theory advanced by the states in ASARCO and Woolworth and adopted here by the New Jersey Supreme Court. In *Container*, this Court stated that in ASARCO: "We held specifically that to accept the State's theory of the case would not only constitute a misapplication of the unitary business concept, but would 'destroy' the concept entirely." *Container* at 177 n.15 (citation omitted).

The court below nevertheless seizes on a footnote in *Container* in an effort to shore up its theory that Bendix's investment in ASARCO was part of Bendix's unitary business because, in the court's eyes, it was part of a "long-term integral operational corporate functio[n]" rather than a "passive investment functio[n]." Pet. App. A 19a. However, the footnote (463 U.S. at 180 n.19) does not support the theory, at least insofar as that theory is relevant to this case.

In the footnote, the Court in *Container* elaborated upon the state court's reliance on the flow of capital resources from Container to its subsidiaries through loans and loan guarantees to support its conclusion that

Container and its subsidiaries were unitary. The footnote states:

There is no indication that any of these capital transactions were conducted at arm's length, and the resulting flow of value is obvious. As we made clear in another context in *Corn Products Refining Co. v. Commissioner*, 350 U.S. 46, 50-53 (1955), capital transactions can serve either an investment function or an operational function. In this case, appellant's loan and loan guarantees were clearly part of an effort to ensure that "[t]he overseas operations of [appellant] continue to grow and to become a more substantial part of the company's strength and profitability."

*Container*, 463 U.S. at 180 n.19 (quoting Container Corporation's 1964 Annual Report 6).

From this the court below reasoned that "[w]hen the investments in affiliates that generate capital gains become an integral part of a corporation's business... a basis is established for making the income from those capital gains subject to a State's apportionable tax formula." Pet. App. A 19a-20a. Assuming *arguendo* the court is correct in its observation that income from investments which are "an integral part of a corporation's business" is apportionable, this does nothing to advance the argument that Bendix's gain from its investment in ASARCO was apportionable. This is because Bendix's investment in ASARCO cannot by any stretch of the imagination be characterized as an "integral part" of Bendix's business. The facts are undisputed that ASARCO "*had nothing to do*" with Bendix's business in an operational sense. Stip. ¶ 62 (J.A. 169) (emphasis added). Accordingly, Bendix's investment in ASARCO cannot be characterized as serving

an "operational function" rather than an "investment function."

No doubt when, as in *Container*, a parent makes non-arm's-length loans to a subsidiary to assure the subsidiary's continuing growth or, in *Corn Products*, when a corn products manufacturer invests in corn futures to assure itself of stable prices for its inventory, the investments are fairly described as "operational" and the income therefrom may be apportioned along with the rest of the income from the taxpayer's business operations. Indeed, the same may be said of many of Bendix's investments in operating companies that enhanced its core businesses. See pp. 30-31, *supra*. But these examples of capital transactions serving an "operational function" have nothing in common with Bendix's minority investment in a company in an unrelated line of business with which Bendix had no functional relationship. Such an investment was aptly described by *Container* itself as an "[i]nvestment in a business enterprise truly 'distinct' from a corporation's main line of business... [which] serves the primary function of diversifying the corporate portfolio and reducing the risks inherent in being tied to one industry's business cycle." *Container*, 463 U.S. at 178.

**E.      Allowing the New Jersey Opinion to  
Stand Would Undermine Fundamental  
Principles of Constitutional Adjudication  
and Deprive Multistate Corporations of  
Meaningful Protection From State  
Taxation of Investment Income**

The mischievous effect of the decision below is not limited to the fact that, if left to stand, it would leave in shambles the principles articulated by this Court in *ASARCO* and *Woolworth*. The collateral consequences of



abandoning these principles would be no less pernicious. One immediate casualty would be the doctrine of *stare decisis*, which this Court has recognized to be "of fundamental importance to the rule of law," *Welch v. Texas Dep't of Highways and Pub. Transp.*, 483 U.S. 468, 494 (1987). See also *Hilton v. South Carolina Pub. Ry. Comm'n*, No. 90-848 (decided December 16, 1991), 60 USLW 4056, 4057, emphasizing "the central importance of *stare decisis* in this Court's jurisprudence."<sup>16</sup> Another casualty would be the existence of meaningful limitations on the states' power to tax the investment income of multistate corporations. The investment income derived by multistate businesses as a result of the rash of acquisitions and divestitures that characterized the American financial markets during the 1980s would become fair game for any state that could claim to identify an "ingrained corporate strategy" that drove the investment decision. This would be true regardless of the connection between the taxpayer's investment and its activities in the taxing state.

Moreover, if the New Jersey court's attempt to extend state taxing powers far beyond the limits heretofore countenanced by this Court were left undisturbed, it would not merely undermine the essential principles of fairness and constitutional restraint on which this Court's unitary business precedents are so soundly based. It

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<sup>16</sup> While this Court has always recognized that *stare decisis* is somewhat less dominant in matters of constitutional interpretation than in matters of statutory interpretation, here there is no plausible reason why a retreat from the principles the Court articulated in the 1980s should be considered. Those cases were fully argued, the opinions carefully explored the relevant issues, and the results reached were a model of fairness and balance under the Constitution. The principles expressed therein should be reconfirmed and reinforced, rather than be subjected to the substantial inroads which New Jersey is seeking to achieve.



would also leave the law in this area in a state of virtual chaos. The latter consequence would be particularly deplorable in light of the significant increase in the scope and size of corporate diversification, which underscores the need for clear and consistent constitutional guidelines from this Court for tax issues raised by cases like this one. Such guidance is essential, in the modern economic setting, to prevent drastic harm from being inflicted on what otherwise would be unchecked and overzealous efforts on the part of the states to make substantial additions to their sources of revenue without regard to the applicable constitutional limitations.

*ASARCO* and *Woolworth* struck a reasonable balance between two competing concerns: the states' legitimate demands for income tax revenues from income-generating activities to which the states accord some benefit, and taxpayers' legitimate demands for protection from state taxing authorities who seek to tax income with which the taxing state has no palpable connection. Unless the New Jersey court's assault on the sound considerations underlying *ASARCO* and *Woolworth* is rebuffed, multistate business will be stripped of real protection from unrestrained state taxation of investment income.

## CONCLUSION

The judgment of the Supreme Court of New Jersey should be reversed with instructions to exclude Bendix's gain from the sale of its ASARCO stock from Bendix's New Jersey apportionable tax base.

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## APPENDIX

### Comparison of the Facts of This Case with the Facts of *ASARCO and Woolworth*

ASARCO and Woolworth were more closely connected to their respective subsidiaries than Bendix was to ASARCO:

- **Ownership**

<i>ASARCO</i>	ASARCO owned about 51.5% of Southern Peru Copper Corp., about 53% of M.I.M. Holdings, Ltd., about 34% of General Cable Corp. and Revere Copper and Brass, Inc., and 49% of Mexicana, S.A. ( <i>ASARCO</i> , 458 U.S. at 309-10).
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<i>Woolworth</i>	Woolworth owned 100% of F.W. Woolworth GmbH (Germany), F.W. Woolworth, Ltd. (Canada), and F.W. Woolworth S.A. de C.V. Mexico, and 52.7% of F.W. Woolworth Co., Ltd. (England) ( <i>Woolworth</i> , 458 U.S. at 356-57).
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<i>Bendix</i>	Bendix owned 20.6% of ASARCO. <i>Stip.</i> ¶ 51 (J.A. 167).
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- **Control**

<i>ASARCO</i>	ASARCO's majority interest, if asserted, could enable it to control the management of Southern Peru, although ASARCO did not actually control Southern Peru;
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ASARCO had the potential to control M.I.M., but there was no claim that it had done so; General Cable, Revere Copper, and Mexicana operated independently of ASARCO, despite ASARCO's substantial ownership interests in those companies (ASARCO, 458 U.S. at 321-24).

*Woolworth* Woolworth elected all of the directors of its three wholly owned subsidiaries and potentially had the authority to operate its subsidiaries as integrated divisions of a single unitary business; Woolworth exercised this control with respect to major financial decisions such as the amount of dividends to be paid and the creation of substantial debt, but not with respect to other matters. (Woolworth, 458 U.S. at 362-69).

*Bendix* Bendix's 20.6% investment in ASARCO did not put it in a position to exercise control over ASARCO, and Bendix did not assert any control. Stip. ¶ 54 (J.A. 168).

- **Line of Business**

*ASARCO* ASARCO's investments were all in companies engaged in essentially the same line of business as

it was—mining, smelting, and refining of nonferrous metals (Southern Peru, copper production; M.I.M. Holdings, mining, milling, smelting, and refining of nonferrous metals; General Cable and Revere Copper, fabrication of metal products; Mexicana, mining and smelting lead and copper) (ASARCO, 458 U.S. at 320-24).

*Woolworth* Woolworth's investments were all in companies engaged in precisely the same line of business—chain store retailing (*Woolworth*, 458 U.S. at 356-57).

*Bendix* Bendix's investment was in a company admittedly engaged in an unrelated line of business. Stip. ¶ 41 (J.A. 164-65).

- **Functional Integration**

ASARCO Southern Peru sold 35% of its copper output to ASARCO; M.I.M. Holdings sold 1% of its output to ASARCO and used an ASARCO melting furnace patent; General Cable purchased approximately 6% of ASARCO's output and ASARCO purchased approximately 0.1% of General Cable's output; Revere Copper purchased approximately 3-4% of



ASARCO's output, and ASARCO purchased approximately 1-2% of ASARCO's output; ASARCO sold Mexicana insignificant amounts of its output and acted as a contract sales agent for Mexicana in the United States (ASARCO, 458 U.S. at 321-24).

*Woolworth*      There was little functional integration, although there was irregular in-person and frequent mail, telephone, and teletype communication between upper echelons of management of the parent and the subsidiaries (*Woolworth*, 458 U.S. at 364-69).

*Bendix*          There was no functional integration. Stip. ¶¶ 41, 62 (J.A. 164-65, 169-71); pp. 7-9, *supra*.